No. 88-408 (2)

Supreme Court, U.S.
FILED
OCT 7 1988
JOSEPH F. SPANIOL, JR.
CLERK

IN THE

# Supreme Court of the United States

OCTOBER TERM, 1988

MIDDLE SOUTH UTILITIES, INC., *et al.*,

*Petitioners*,

—v.—

RITA ISQUITH, *et al.*,

*Respondents.*

## BRIEF IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

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RITA ISQUITH, *et al.*,

*Respondents.*

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## BRIEF IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

Respondents, Rita Isquith, f/b/o Fred Taylor Isquith, Jr., Monroe Weintraub, George M.D. Richards, Virginia A. Richards, David Winston, Franklin Plant and Sonny Merritt, herewith submit their brief in opposition to the Petition for Writ of Certiorari submitted by Middle South Utilities, Inc. ("MSU"), seeking review of the decision and opinion of the United States Court of Appeals for the Fifth Circuit in this case. The Fifth Circuit's opinion is reported at *Isquith v. Middle South Utilities, Inc.*, 847 F.2d 186 (5th Cir. 1988).

## COUNTERSTATEMENT OF THE CASE

Neither the District Court decision granting summary judgment nor the Fifth Circuit reversal of that decision have anything to do with respondents' alleged inability to prove loss causation, *i.e.*, that their losses on investments in MSU stock

were in whole or in part caused by petitioners' false or misleading statements to the investing public. Nor does the decision proposed for review undermine *Celotex Corp. v. Catrett*, 477 U.S. 317 (1986). The Petition herein tries to create an issue which does not exist in this case. The central issue discussed in each of the decisions below is *materiality*, a mixed question of law and fact under *TSC Industries, Inc. v. Northway, Inc.*, 426 U.S. 438 (1976) and *Basic, Inc. v. Levinson*, ____ U.S. ____, 108 S. Ct. 978 (1988).

The District Court, on a record uncluttered by much in the way of evidence (since respondents were largely occupied with defending their pleading and had only just begun document discovery), determined that MSU's public documents contained no material misrepresentations. The Fifth Circuit disagreed, finding, among other things, that such a determination required a more thorough review of the evidence. Under *Northway* and *Basic*, the Fifth Circuit was correct. The Petition thus presents no conflict requiring the attention of this Court.

The original Complaint in this case was filed on August 19, 1985, in the United States District Court for the Eastern District of Louisiana.[1] Respondents later filed a Consolidated Amended and Supplemental Class Action Complaint (the "Complaint") against Middle South Utilities, Inc. and certain of its subsidiaries, MSU officers and directors and auditors, as well as underwriters of a MSU stock offering.

Respondents charge in the Complaint that petitioners engaged in an ongoing course of conduct whereby they misrepresented and concealed from the investing public a number of material facts in violation of Section 11 or 15 of the Securities Exchange Act of 1933 ("1933 Act") and Section 10(b) or 20

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1 Plaintiff Rita Isquith f/b/o Fred Taylor Isquith, Jr., UGMA, filed her complaint in the United States District Court for the Eastern District of Louisiana. Subsequently, plaintiffs Monroe Weintraub, George M.D. Richards, Virginia Richards, Franklin Plant and Sonny Merritt filed similar class action complaints between August 20, 1985 and September 19, 1985. All five actions were consolidated for pre-trial purposes by order of the District court entered October 23, 1985.

of the Securities Exchange Act of 1934 ("1934 Act"), thereby artificially inflating the price of MSU stock purchased by investors pursuant to a registration statement and prospectus dated June 7, 1984, pursuant to the MSU Dividend Reinvestment and Stock Purchase Plans and in the open market between March 30, 1983 and August 16, 1985.[2]

Respondents filed a motion for certification of three plaintiff classes: the Dividend Reinvestment Class, the June 7, 1984 Prospectus Class, the Open Market Class, and a defendant class of underwriter defendants for the June 1984 Prospectus Class.

On April 18, 1986, MSU and its subsidiaries, the present and former officers and directors filed a Motion to Dismiss, or in the alternative, for Summary Judgment. On April 30, 1986 the underwriter defendants filed a motion to adopt and join in the Motion to Dismiss filed by MSU. Thereafter, on June 6, 1986, Deloitte, Haskins & Sells, MSU's auditors, filed a separate Motion to Dismiss, or in the alternative for Summary Judgment.

Petitioners all sought to dismiss the Complaint asserting that they had made full disclosure of all material facts, and did not misrepresent or omit any of the negative investment facts which

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2 The misrepresentations and non-disclosures of material facts relate to MSU's planning and construction of two nuclear projects, Grand Gulf Station (Grand Gulf I and Grand Gulf II) and Waterford II. Respondents' Complaint details the alleged misrepresentations and non-disclosures with regard to:

1. MSU's overstatement of demand for generating capacity from Waterford and Grand Gulf;

2. MSU's ability to obtain adequate and timely rate relief from state regulatory agencies for the cost to construct these projects;

3. The factual basis for the cost and completion estimates regarding these projects;

4. MSU's falsely inflated reported income because of the improper inclusion of AFUDC income;

5. The effect that failure to recover the cost of construction by rate increases would have on MSU's ability to continue paying dividends.

Complaint, ¶¶ 3 and 79.

respondents claim were misrepresented or omitted. In support of their motions, petitioners submitted evidence consisting of only portions of certain MSU public filings and analysis reports covering a period of over two years. In a four page Order and Reasons dated January 6, 1987, the District Court granted the motions of petitioners, deeming them motions for summary judgment. The District Court failed to consider the individual misrepresentations and omissions alleged by respondents. The District Court determined that, based on its review of the documents submitted by defendants and the portions of MSU statements cited by plaintiffs in the Complaint, that petitioners had, as a matter of law and indisputable fact, fairly informed the investing public. Significantly, the District Court did not consider it necessary to have before it or to review complete MSU documents or other information available to the public at the time of an alleged misrepresentation by MSU, nor to consider the total mix of information available to investors with regard to each alleged misrepresentation and omission during the period covered by the Complaint. The District Court explained:

> Plaintiffs have leveled serious charges, and they have been seriously considered. We stress this to dispel any contrary inference which may otherwise result from the brevity of these reasons. An appeal is virtually certain, and it would be a waste of judicial resources for us to write at length, or even at all, on every point raised by these motions.

App. 49a.[3]

Contrary to the District Court's conclusion, the United States Court of Appeals for the Fifth Circuit held that the context in which disclosures are made and the total mix of information must be considered when evaluating allegations of non-disclosures and misrepresentations of material facts. The Fifth Circuit correctly observed that the issue of whether the MSU disclosures were adequate is governed by the standard for materiality adopted by this Court in *TSC Industries, Inc. v. Northway, Inc.*, 426 U.S. 438, 439 (1976). App. 37a-38a.

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3 The Appendix to petitioners' Petition for a Writ of Certiorari is cited herein as "App. _____".

Although potentially time consuming, the Court of Appeals specifically instructed that the District Court on remand, if it elected to grant summary judgment, do precisely what it chose not to do when deciding petitioners' motions:

> [W]e would have to determine, for each disclosure challenged, the scope of Middle South's disclosure duty and the extent of Middle South's actual disclosure, and decide whether any discrepancy existed between what should have been disclosed and what was disclosed.
>
> . . . On remand, however, the district court has more than one option, it can remain on the same procedural course or reevaluate, with the benefit of certain corrections we have made, the defendants are entitled to judgment as a matter of law. If the court elects to follow this path and once again to enter summary judgment for the defendants, it should provide a detailed analysis supporting that result so that the reviewing court can properly perform its function.

App. 44a-45a.

As the Fifth Circuit correctly found, since materiality is a mixed question of law and fact under *Northway*, it is necessary that judge or jury acting as trier of fact make these admittedly difficult individual determinations in order to arrive at a fair verdict. If such a task is complicated here, it is because this is a complex action in its early stages. As is often the case, discovery may result in a narrowing of issues. Before discovery is substantially complete, however, such determination of materiality, which must be based on evidence of the truth or falsehood of the statements in question, is inappropriate if not impossible.

The Court of Appeals further rejected the District Court's determinations that (a) published predictions are immune from the antifraud protections of the securities laws and (b) the way in which information is conveyed to potential investors need not be considered when examining the adequacy of disclosures. App. 42a. By relying on erroneous standards, the District Court

incorrectly concluded that petitioners were entitled to judgment as a matter of law.

## REASONS FOR DENIAL OF THE WRIT

### Certiorari Should Be Denied Because The Court of Appeals Correctly Found That The District Court Improperly Decided Factual Issues of Materiality Utilizing Incorrect Legal Standards

**1. The Court of Appeals did not fail to give effect to this Court's decision in *Celotex Corp. v. Catrett*, 477 U.S. 317 (1986).**

The petition filed in this action presents the common plea of dissatisfied litigants that the court below committed an error which this Court should now correct. As Chief Justice Vinson once stated, however, this Court "is not, and never has been, primarily concerned with the correction of errors in lower court decision."[4] Rather, the Court decides cases presenting issues of national importance. No such issue is presented in this case.

Petitioner's argument that the Court of Appeals' decision either fails to give effect to, or serves to undermine, this Court's decision in *Celotex Corp. v. Catrett*, 477 U.S. 317 (1986), is simply not supported by the record.

*Celotex* was decided by the District Court for the District of Columbia after discovery had been conducted. That Court granted summary judgment to defendant Celotex because the plaintiff failed to show, after discovery, that her husband had been exposed to defendants' asbestos products. The Court of Appeals for the District of Columbia reversed on the grounds that the defendant failed to provide evidence that plaintiff could *not* show causation. This Court, in a 5 to 4 decision, reversed and remanded, holding that a moving party, under Rule 56 of the Federal Rules of Civil Procedure, was not required to supply evidence negating an opponent's claim, but

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4 Address by Chief Justice Vinson before the American Bar Association, September 7, 1949, 69 S.Ct. v, vi (1949).

might discharge its Rule 56(c) "showing" by "pointing out to the district court that there is an absence of evidence to support the non-moving party's case." *Celotex*, 471 U.S. at 325.

Since no substantial discovery has yet been taken in this action, and because most, if not all, of the evidence is in the hands of defendants, the instant action is in an entirely different posture than *Celotex*. Neither petitioners nor respondents have submitted "evidence" on the motion, in the sense of internal documents, depositions, affidavits, or otherwise. Only portions of publicly available documents were proffered by petitioners and cited in respondents' Complaint. This was the only evidence before the District Court.

Respondents argued the motions first as Rule 12(b) motions to dismiss, and requested the opportunity to make further submissions, preferably after discovery was complete, if the District Court chose to consider the motions under Rule 56. However, respondents also argued that the evidence proferred by defendants did not demonstrate that full disclosure was made by MSU, and that the evidence, such as it was, might just as easily support a contrary conclusion.

The Court of Appeals concluded that respondents were free to argue from petitioners' evidence rather than submitting their own. App. 19a-21a. Thus, the Court of Appeals has not contradicted *Celotex*, either in its discussion of Rule 56 standards or in its quite limited concern with proof of causation.

**2. The substantive issue presented to, and decided by, both the District Court and the Court of Appeals was materiality, not loss causation.**

The substantive issue presented to, and decided by, the two lower courts was not loss causation, an issue petitioners have belatedly raised here. Rather, the substantive issue decided was materiality, as defined in *Northway*.

The Court of Appeals noted that:

> The thrust of defendants' argument [in the District Court] was that, as a matter of law, defendants did not misrepre-

> sent or omit any material information from the documents it filed with the SEC and disseminated to its shareholders.

App. 10a.

The Court of Appeals further recognized that:

> the district court found that "a reasonable potential investor who would have read any of [the] documents [upon which plaintiffs base their claims] as a whole would have been fairly informed about the negative investment factors which plaintiffs contend were misstated or omitted by defendants."

App. 7a. In *Northway*, this Court defined materiality in terms of the omitted (or misstated) facts having been "viewed by the reasonable investor as having altered the 'total mix' of information made available." 426 U.S. at 449. Therefore, it is clear, as the Court of Appeals concluded, that the District Court's conclusion of adequate disclosure was one based on materiality. App. 37a-38a.

The issue of loss causation was not presented to the Court of Appeals. The Middle South Utilities petitioners set forth this sole substantive issue[5] in the Court of Appeals:

> 1. Whether the district court properly granted summary judgment in favor of [petitioners] because the undisputed record established that MSU's disclosures clearly informed a reasonable investor of the matters allegedly undisclosed.

Brief of Middle South Utilities in the Court of Appeals, at 1. Similarly, petitioner Deloitte Haskins & Sells failed to raise the loss causation issue[6] in the Court of Appeals, raising only the

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5 Two procedural issues—neither of which mentioned or implied loss causation—were also presented to the Court of Appeals by the Middle South Utilities petitioners. Brief of Middle South Utilities in the Court of Appeals at 1-2.

6 Petitioner Deloitte Haskins & Sells also presented a procedural issue to the Court of Appeals. Again, loss causation was neither mentioned or implied by this issue. Brief of petitioner Deloitte Haskins & Sells in the Court of Appeals at 1.

substantive issue of adequacy of disclosure. Brief of petitioner Deloitte Haskins & Sells in the Court of Appeals at 1-2.

It is this Court's normal practice to refrain from addressing issues not raised in the Court of Appeals. *Equal Employment Opportunity Commission v. Federal Labor Relations Authority*, 476 U.S. 19 (1986). While respondents recognize that this Court, on occasion, has departed from this normal practice, such departure is reserved for exceptional cases. *Heckler v. Campbell*, 461 U.S. 458, 468 n.12 (1983); *McGoldrick v. Compagnie Generale Transatlantique*, 309 U.S. 430, 434 (1940). This is not such a case.

**3. The decision by the Court of Appeals correctly applied the applicable standards of materiality and adequate disclosure.**

The Court of Appeals properly characterized materiality and adequate disclosure as mixed questions of law and fact—questions which "are particularly ones for the trier of fact." *TSC Industries, Inc. v. Northway, Inc.*, 426 U.S. at 450. App. 38a-39a. The Court of Appeals noted that summary judgment is appropriate only if "the disclosure is so obvious that reasonable minds cannot differ." App. 39a. *TSC Industries, Inc. v. Northway, Inc.*, 426 U.S. at 450. Based on the record below, the Court of Appeals properly decided that it was not.

The Fifth Circuit rejected several conclusions upon which the District Court's decision was based. The Court of Appeals rejected the District Court's conclusion that respondents' allegations "divide unequivocally into a discrete list of 'negative investment factors,' " and recognized that those allegations were "interdependent, susceptible to interpretation and, therefore, capable of being characterized in more than one way." App. 40a.

The Court of Appeals criticized the District Court's failure to differentiate between predictions made by the Middle South Utilities petitioners in the disclosure document and those which were not disclosed. The former may be " 'facts' " subject to liability under the securities laws. App. 30a. *See, e.g., Marx v. Computer Sciences Corp.*, 507 F.2d 485, 489 (9th Cir. 1974).

Similarly, the Court of Appeals rejected the District Court's conclusion that the manner of presentation cannot serve as a basis for liability. App. 29a. *See, e.g., Greenapple v. Detroit Edison Co.*, 618 F.2d 198, 205, 210 (2d Cir. 1980); *Smallwood v. Pearl Brewing Co.*, 489 F.2d 579, 605 (5th Cir. 1974); *Gerstle v. Gamble Skogmo, Inc.*, 478 F.2d 1278, 1297 (2d Cir. 1973); *Feit v. Leasco Data Processing Equipment Corp.*, 332 F. Supp. 544, 565 (E.D.N.Y. 1971); *Gould v. American Hawaiian Steamship Co.*, 331 F. Supp. 981 (D. Del. 1971). Based upon these conclusions, the Fifth Circuit quite properly determined that summary judgment could not be sustained on the record before the Court.

**4. This case does not warrant review at this stage of the proceedings.**

This case arises from petitioners' filing of a motion to dismiss, pursuant to Rule 12(b)(6), Fed. R. Civ. P., with an alternative prayer for summary judgment, pursuant to Rule 56, Fed. R. Civ. P. At the time that briefing of this motion was concluded, respondents had just begun to review documents produced by the Middle South Utilities petitioners in response to respondents' request for production of documents.[7] By the time of the District Court's entry of summary judgment, respondents had produced only a few thousand of the approximately 7 million pages estimated by petitioners to be responsive to respondents' request for production. Brief of respondents in the Court of Appeals, filed August 3, 1987, at 19-20 and n. 3.

*Celotex* requires adequate time for discovery before summary judgment may be entered. 477 U.S. at 322. Respondents were not afforded adequate time. The Fifth Circuit made clear that respondents' complaint satisfies the requirements of Rule 12(b)(6). App. 12a, n.3. On this record, the Petition should be denied and respondents should be permitted to proceed with prosecution of this action.

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7 No documents were produced by petitioner Deloitte Haskins & Sells, or by petitioners Morgan Stanley & Co., First Boston Corp. and Merrill Lynch Capital Markets.

## CONCLUSION

It is respectfully submitted that petitioners have failed to sustain their burden of establishing that there are special and important reasons why the Writ of Certiorari should be granted. The decision below does not conflict with any decision of another Circuit, or of this Court. As the decision of the Fifth Circuit correctly applies principles previously articulated by this Court, it does not involve any important question of federal law which has not been, but should be, settled by this Court. Accordingly, petitioners have not shown any reason why this Court should exercise its sound judicial discretion to entertain this case.

Dated: October 7, 1988

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